

# Office of the Indiana Secretary of State Connie Lawson



## Indiana Securities Division

# **Connie Lawson**

## **Indiana Secretary of State**

**Alex Glass**

**Indiana Securities Commissioner**

# The Indiana Securities Division

**Mission: Protect Investors and Maintain a Competitive Marketplace**

The Indiana Securities Division regulates:

- Registered Investment Advisers & Investment Adviser Representatives
- Broker-Dealers
- Broker-Dealers and Broker-Dealer Agents
- Mortgage brokers
- Collection agencies
- Franchisors
- Continuing Care Retirement Contracts
- Security Products

# **Indiana Registered Investment Adviser Examinations**

**Teaune Trice  
Examiner**

# Indiana RIA Exams

## What to Expect

### GOAL:

- To protect investors and legitimate businesses in Indiana.
- Two Types of Examinations:
  - Routine
  - For Cause
- Examinations generally will be conducted where the books and records are located

# Indiana RIA Exams

## What to Expect

- Routine exams are typically a four-part process
  - Pre-Exam
  - On-Site
  - Post-Exam
  - Resolution
- Usually one - perhaps two examiners

# Indiana RIA Exams

## What to Expect/Pre-Exam

- Notification of upcoming exam typically done by e-mail at least two weeks in advance with a list of documents to have available
- A request to delay an examination date is granted only on an exception basis and must be in writing
- Some exams may be unannounced

# Indiana RIA Exams

## What to Expect/On-Site

- During the on-site portion of exam the Division typically requests that the firm's Point of Contact be available the entire day
- Initial interview conducted by examiner
  - Tour of the office
  - Interview: questions about your business and business practices

# Indiana RIA Exams

## What to Expect/On-Site

- Be prepared with requested documents readily available  
(See **710 IAC 4-9-7**)
- Have key personnel available to answer questions
- Exit interview (optional)
  - The examiner explains what comes next. May be done onsite or may come after the actual visit, but not required.

# Indiana RIA Exams

## Books and Records

- **710 IAC 4-9-7**, the Indiana Administrative Code, gives the books and records required by the State of Indiana for Registered Investment Advisers
- Failure to keep accurate books and records can be an indication of unethical business practices

# Indiana RIA Exams

## What to Expect/Post-Exam

- Once examiner has left the office, the exam is not over
  - Frequently the examiner requests additional documents or information from the RIA or the custodian
- May take several weeks depending on responses from RIA and/or custodian
- Once post-exam work is complete, an exam report is prepared

# Indiana RIA Exams

## What to Expect/Resolution

- No further action required
- Deficiency/cautionary letter may be sent
  - Registrant must respond to the deficiency/cautionary letter in writing, by the deadline provided
  - Once all deficiencies have been satisfactorily addressed, exam is closed
- Certain issues may be referred to enforcement for action or investigation

# Indiana RIA Exams

## Common Exam Deficiencies\*

- Incomplete, inadequate, or no contract with clients
- Incomplete or no written supervisory/compliance procedures if more than one employee
- Non-compliance with supervisory procedures
- Failure to offer/document offer to send disclosure documents annually

*\*Any could result in enforcement action*

# Indiana RIA Exams

## Common Exam Deficiencies\*

- Inaccurate or incomplete Forms ADV Part 1 or 2
  - Failure to update for material changes and/or annually
- Fee Inconsistencies between Part 2 and client agreement
- Fees charged are greater than the amount in contract

# Indiana RIA Exams

## Best Practices

- Prepare separate fee statements for clients showing valuations, calculations and amount
- Review and update all contracts, as needed
- Prepare and maintain client profiles, including suitability
- Prepare and maintain all required records including financial records
- Keep accurate financial records

# Indiana RIA Exams

## Best Practices

- Back-up electronic data and protect records
- Prepare and keep a business continuity plan updated  
(see North American Securities Administrators Association handout)
- Complete a compliance review at least annually
- Prepare and distribute a privacy policy initially and annually

# Indiana RIA Exams

## Best Practices

- Review and revise all advertisements, including website and performance advertising, for accuracy
- Implement appropriate custody safeguards, if applicable
- Review solicitor agreements, disclosure and delivery procedures

# **ADV Part 1 and 2**

**Ashlie Gerrish**  
**Senior Examiner**

# ADV Part 1

## General Information

- Check the box/fill in the blank format
- Used for registration
- Available to the public on broker check

# ADV Part 1

## Components

- Part 1A – Basic Form
- Part 1B – State Registration
- Schedule A – Direct Owners and Executive Officers
- Schedule B – Indirect Owners
- Schedule C – Used to Amend Schedule A and B
- Schedule D – Additional Firm Information

# ADV Part 2

## General Information

- Narrative format
- Client disclosure
  - Scope of services
  - Fees
  - Conflicts
- Provided to all prospective clients and offered to all existing clients within 120 days of the firm's yearend

# ADV Part 2

## Components

- Part 2A – Firm Disclosure
- Part 2B – IAR Disclosure
- Appendix 1 – Wrap Brochure

# ADV Part 1

## Common Deficiencies

- Item 5A and 5B
- Item 5F
  - *“Continuous and regular supervisory or management services to securities portfolios”*
- Item 6A
  - Other Business Activities

# ADV Part 2

## Common Deficiencies

- ADV Part II rather than ADV Part 2
- “Registered with the U.S. Securities and Exchange Commission”
- Inconsistencies between the Part 1 and Part 2

## ADV Part 2

Topic	ADV Part 1 Item	ADV Part 2 Item
Services Provided	Item 5G	Item 4
Types of Clients	Item 5D	Item 7
Assets Under Management	Item 5F	Item 4
Wrap Program	Item 5I	Item 4D (If the firm offers a wrap program, Appendix 1 is also required)

# Annual Requirements

## Updates

- Both Part 1 **AND** Part 2 must be updated annually (within 90 days of your fiscal year end)
- If “material” information on the Part 1 or any section of the Part 2 becomes inaccurate or misleading, an other-than-annual amendment must be filed
  - **710 IAC 4-9-16 (c)**
- Annual Securities Division Questionnaire required to be completed annually by March 31<sup>st</sup>

# **Custody**

**Ashlie Gerrish**  
**Senior Examiner**

# Custody

## Definition

You or a related person holds, directly or indirectly, client funds or securities or have any authority to obtain possession of them in connection with advisory services you provide to clients.

# Custody

## Examples

- You direct deduct fees from a client's account
- You accept third party checks or securities from a client
- You accept client fees of \$500 or more six months or more in advance
- You manage a private fund (i.e. hedge fund)

PRACTICE	REQUIREMENT
Accept 3 <sup>rd</sup> party checks or Securities	Maintain blotter showing date received & date forwarded
Accept fee payment of >\$500 more than 6 months in advance.	Submit audited balance sheet of firm annually OR Have independent public accountant conduct a surprise audit
Only manage a private fund	Submit audited balance sheet of the fund OR Have independent public accountant conduct a surprise audit
Manage a private fund and has clients outside of them fund	Submit audited balance sheets of the firm <u>AND</u> fund OR Have independent public accountant conduct a surprise audit

# Custody

## Additional Issues

- Credit Card Payments
  - How is account information stored
- Acting as Trustee
- Acting as Executor
- Access to Client Accounts
  - Is client log in information being used to access client accounts

# Custody

## Client Account Access

- Can be considered custody
  - Ability to withdraw funds
  - Ability to change address
  - Ability to change beneficiary
- More than just a custody issue
  - User Agreement Violation
  - Online Fraud Policy Violation

# **Ethics, Fiduciary Duty & Senior Safe: Relating to Diminished Capacity**

**Jennifer Sisson**  
**Examiner**

# Fiduciary Duty

## Definition

A legal obligation of one party to act in the best interest of another

# Fiduciary Duty/Ethics

## The Fundamental Nature of the Relationship

An adviser's relationship with its clients is fundamentally one of "trust and confidence."

# Fiduciary Duty/Ethics

## Duty of Care

- Exercise due care (reasonableness/prudence)
- Use reasonable care to avoid misleading clients
- Have a reasonable basis for investment advice
- Seek best execution of client trades

# Fiduciary Duty/Ethics

## Duty of Loyalty

- Act in the best interest of clients
- Put the client's interest first
- Put the client's interest ahead of adviser's
- Avoid (or mitigate) conflicts of interest
- Avoid using client's assets to benefit adviser
- Avoid self-dealing

# Fiduciary Duty/Ethics

## Duty to Act in Obedience

- Adhere to governing documents
- Trust instrument
- Investment mandate
- Follow client instructions and guidelines
- Impermissible investments
- Directed brokerage
- Account handling instructions

# Fiduciary Duty/Ethics

## Duty to Act in Good Faith

- Act honestly with candor and utmost good faith
- Treat clients fairly
- In general
- Avoid favoritism of one client/group over another

# Fiduciary Duty/Ethics

## Duty of Disclosure

- Full and fair disclosure of all material facts
  - “material” = a reasonable investor ought to know in order to make an informed decision
- Avoid misleading clients
  - avoid partial truths, exaggerations, unwarranted claims, misleading impressions

# Fiduciary Duty/Ethics

## What is Financial Exploitation?

- Senior financial exploitation and fraud is the illegal or improper use of a senior's resources for another's profit or advantage
  - **Exploitation** usually involves someone the senior knows, such as a family member or caregiver
  - **Fraud** is usually perpetrated by a stranger, such as a telemarketer or investment promoter

# Fiduciary Duty/Ethics

## Issues Facing Financial Professionals

- Appropriateness of investment products
- Effective communication with older clients who may have physical or sensory challenges
- Diminished capacity to make decisions and execute transactions
- The potential for fraud and abuse by trusted family members, friends, or strangers

# Fiduciary Duty/Ethics

## You Can Play a Key Role in Stopping Financial Exploitation

- Regular contact puts you in a unique position to detect behavior changes and to assist in protecting customers before assets have been disbursed
- Proactive measures help to promote goodwill within the communities where you have footprints
- Reporting is consistent with your role in protecting assets, preventing losses, and safeguarding customer information

# Fiduciary Duty/Ethics

## Best Practices When Dealing With Seniors

### Ongoing

- May encourage investors who are in good health to discuss financial affairs with trusted family members or attorney to ensure financials are handled properly in case of future health issues
- Document conversations with investors
- Send follow-up letters to the investors after the conversation to reiterate what was discussed

# Fiduciary Duty/Ethics

## Best Practices When Dealing With Seniors

### As A Firm

- Discuss “senior issues” with staff
- Develop “issues, symptoms, alternatives” list
- Establish policies for escalating Issues in cases of diminished capacity
- Review products for appropriateness for senior investors
- Take time to discuss and develop age-based restrictions on certain products.
- Include risks related to senior investors in your annual risk assessment

# CONTACTS

**Indiana Secretary of State Connie  
Lawson  
Securities Division  
302 West Washington Street,  
Room E-111  
Indianapolis, IN 46204**

**Phone: (317)232-6681  
Fax: (317)233-3675  
Web Site: [www.sos.in.gov](http://www.sos.in.gov)**

**Commissioner**

**Alex Glass: [aglass@sos.IN.gov](mailto:aglass@sos.IN.gov)**

**(317) 232-6681**

**Chief Deputy Commissioner**

**Noelle Sykes: [nsykes@sos.IN.gov](mailto:nsykes@sos.IN.gov)**

**(317) 232-6681**

**Senior Examiner**

**Ashlie Gerrish:  
[agerrish@sos.IN.gov](mailto:agerrish@sos.IN.gov)**

**(317) 234-7902**

**Examiners**

**Jennifer Sisson:  
[jsisson@sos.IN.gov](mailto:jsisson@sos.IN.gov)**

**(317) 234-8974**

**Teaune Trice:  
[tatrice@sos.IN.gov](mailto:tatrice@sos.IN.gov)**

**(317) 903-6475**